LING BENG HUI & ORS.

v.

LING BENG SUNG

HIGH COURT BORNEO
HAIDAR MOHD. NOOR J
[SUIT NO. 19 OF 1989]
26 OCTOBER 1989

COMPANY LAW: *Conflict of interest of a company director - Locus standi of interested parties - Whether there was breach of fiduciary duty.*

The plaintiff in the present case filed an application to intervene in suit no. 17 of 1989, such application is yet to be heard. In suit no. 17 of 1989, Ming Yueh Holdings Sdn. Bhd. ('Ming Yueh') is the plaintiff and Kong Ming Bank Berhad ("the bank") and Mayban (Nominees) Sdn. Bhd. ('Mayban') are the defendants. In suit no. 17, Ming Yueh is claiming its rights to 785,699 shares in the bank and other attendant reliefs. The said shares are also the subject matter in suit no. 23 and 34 of 1984.

An interim injunction was granted to Ming Yueh earlier to restrain the bank from holding an annual general meeting (AGM), extraordinary general meeting (EGM) or any other meetings unless Ming Yueh is given notice, allowed to attend and vote at the meetings, this injunction set aside by this Court on the primary ground that Ming Yueh not being the registered member on the company's register at the time of the application for an interim injunction, had no *locus standi* to ask for such an interim injunction.

When the summons came up for hearing, Mr. Wong (Counsel for the defendants) raised a preliminary objection on the grounds that the plaintiffs have no *locus standi* or competency to institute the present proceedings and that no cause of action arose in this case i.e. no substantive relief prayed for.

The plaintiffs complained that in view of the defendants dual position and interests in Ming Yueh and the bank, the defendant should not participate in the board's deliberations/decisions in respect of suit nos. 17 of 1989, 23 and 34 of 1984 such as the defences of the bank and appointments of solicitors/senior Counsels etc.

Held:

[1] The justice of the case requires the defendant to declare his interests and refrain from participating and voting in matters relating to suits which Ming Yueh is a party.

[2] The plaintiffs as shareholders of the bank have the *locus standi* to institute the present proceeding.

[3] As the defendant is in breach of his fiduciary duty and acting in conflict of interest the amended statement of claim does disclose a cause of action against the defendant.

[Order accordingly.]

Cases referred to:

Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No.2) [1982] Ch 204
Edwards v. Halliwell [1950] 2 All ER 1064
Lennard's Carrying Company v. Asiatic Petroleum [1915] AC 705
H.L. Bolton Co. v. T.J. Graham & Sons [1956] 3 All ER
Rayfields v. Hands [1960] Ch 1
Wong Kim Fatt v. Leong & Co. Sdn. Bhd. [1976] 1 MLJ 140

Legislation referred to:
Rules of the High Court 1980, O. 20
Companies Act 1965, s. 33(1)

Other sources referred to:
Gower's Principles of Modern Company Law, 4th Edn. at p. 210
Walter Woon on Company Law, Robert R. Penington 5th Edn at p. 727
The conduct of Meeting by John Yelland of p. 55

For the plaintiffs/applicants - C. Abraham with Willaim Lau; M/s. Lau & Co. Advocates
For the defendant/respondent - Richard Wong Ho Leong; M/s. Siong & Wong Advocates

JUDGMENT

Haidar Mohd. Noor J:

The plaintiffs filed this Suit No. 19 of 1989 against the defendant on 17 May 1989. On 5 June 1989 the plaintiffs filed the amended statement of claim. There is nothing on record to show under what provisions or order the amended statement of claim was filed by the plaintiffs. I take it that the amended statement of claim was filed pursuant to O. 20 of Rules of the High Court 1980, that is, without the leave of the Court or at any time before the pleadings are deemed to be closed.

According to para. 23 of the amended statement of claim, the plaintiffs claim for:

(i) A declaration that the defendant has a vested interest in the outcome of Suit Nos. 17 of 1989, 23 of 1984 and 34 of 1984 and hence the defendant should refrain from participating in any discussions and/or decisions to be made by the board of directors in respect of the afore-mentioned suits and should be restrained from voting on issues concerning the said suits as per the provisions of Article 73 of the memorandum and articles of association of the bank.

(ii) An injunction restraining the defendant whether by himself, his servant or agent or proxy, or otherwise howsoever from attending participating in any discussions on the agenda and/or voting at the said directors meeting to be held on 9 June 1989 at 3 p.m. at No. 21, Wong Nai Siong Road, Sibu particularly in so far as it relates to Sibu High Court Suit No. 17 of 1989.

(iii) An injunction restraining the defendant whether by himself, his servant or agent or proxy, or otherwise howsoever from attending participating in any discussions and/or voting at any directors meeting to be held in the future in so far as it relates to matters arising from or connected in anyway whatsoever with decisions to be made or resolved in respect of Sibu High Court Suit Nos. 17 of 1989, 23 of 1984 and 34 of 1984.

(iv) An injunction restraining the defendant whether by himself his servant or agent or proxy, or otherwise howsoever from doing any other acts at any board of directors meeting which may prejudice the interest of the bank.

(v) Damages

(vi) Costs

(vii) Such further or other relief as this Honourable Court may deem fit and just in the circumstances.

On 8 June 1989, the plaintiffs filed a summons in chambers (Encl. 16) seeking for the following orders:

(i) An injunction to restrain the defendant from voting at the board of directors meeting of the Kong Ming Bank Berhad (hereinafter called the Bank) to be held on 9 June 1989 at 3.00 p.m. at No. 21, Wong Nai Siong Road, Sibu, in so far as it relates to Sibu High Court Suit No. 17 of 1989.

(ii) An injunction to restrain the defendant from voting at any board of directors meeting of the bank to be held in the future in so far as it relates to matters arising from or connected in anyway whatsoever with decisions to be made or resolved in connection with Sibu High Court Suit No. 17 of 1989.

(iii) An injunction to restrain the defendant from voting at any board of directors meeting of the bank to be held in the future in so far as it relates to matters arising from or connected in any way whatsoever with decisions to be made or resolved in connection with Sibu High Court Suit Nos. 23 of 1984 and 34 of 1984.

(iv) That the costs of this application be provided for.

The summons is supported by the affidavit of the second plaintiff, Dato Ling Beng King and also on behalf of the other plaintiffs.

The summons and the writ of summons with the amended statement of claim were personally served on the defendant on 8 June itself (Encl. 18 and 19). As the summons and the writ were served late on the defendant, Mr. Wong, Counsel for the defendant sought an adjournment and the application was granted with an undertaking by Mr. Wong that no consideration and decision will be taken on item 2 of the agenda of the board of directors meetings of the Kong Ming Bank Berhad till after disposal of the summons. The summons was accordingly adjourned to 11 August 1989.

When the summons came up for hearing before me on 11 August 1989, Mr. Wong raised a preliminary objection on the following grounds:

(1) *Locus standi* or the competency of the plaintiffs to institute the present proceeding.

(2) No cause of action arising in this case, i.e. no substantive relief prayed for.

Mr. Wong urged the Court to deal with his preliminary objection first without going into the merits of the case and relied on the case of *Prudential Assurance Co. Ltd. v. Newman Industries Ltd. (No. 2)* [1982] Ch 204 where the Court of Appeal held that the proper course in a derivative action was for the Judge to settle the question of the plaintiff's standing as a preliminary issue before hearing the main case on the merits and not defer his ruling until after hearing the case on the merits. A plaintiff ought to be required before proceeding with his action to establish a *prima facie* case (1) that the company is entitled to the relief claimed, and (2) that the action falls within the "proper boundaries" of the exception to the rule in *Foss v. Harbottle.*

Before proceeding further, it would be appropriate, I think, for me to set out briefly the claims and the parties involved in respect of suit nos. 17 of 1989, 23 of 1984 and 34 of 1984 referred to in the amended statement of claim in this case.

In suit no. 17 of 1989, Ming Yueh Holdings Sdn. Bhd. (Ming Yueh) is the plaintiff and Kong Ming Bank Berhad ('the bank') and Mayban (Nominess) Sdn. Bhd. ('Mayban') are the defendants. The plaintiffs in the present case filed in an application to intervene in suit no. 17 of 1989, such application is yet to be heard. However, the interim injunction granted to Ming Yueh earlier on restraining the bank from holding an annual general meeting, extra-

ordinary general meeting or any other meetings unless Ming Yueh is given notice and allowed to attend the meetings and vote thereat was set aside by me on the primary ground that Ming Yueh, not being the registered member on the record of the company's register at the time of the application for an interim injunction, had no *locus standi* to ask for such an interim injunction. Thus, the passage is cleared for the bank to proceed with its meetings. I am advised that there has been no appeal against the lifting of the said interim injunction by me. Now, in suit no. 17 of 1989 Ming Yueh is claiming its rights to the 785,699 shares in the bank and other attendant reliefs and the said shares is the subject matter of a dispute in suit nos. 23 and 34 of 1984 (see JK-19 and JK-20). In suit no. 23 of 1984 Ming Yueh and Datuk Ling Beng Sung are cited as the defendants together with Chahaya Construction and Development Sdn. Bhd. by Abang Mohamed bin Abang Sarkawi. In suit no. 34 of 1984 Ming Yueh and Datuk Ling Beng Sung are also cited as the defendants together with Chahaya and also the bank by Fusing Construction Sdn. Bhd. It is not disputed that Datuk Ling Beng Sung is the chairman, director and shareholder of the bank as well as the chairman, director and shareholder of Ming Yueh. In suit nos. 23 and 34 of 1984 the real battle is for the 785,699 shares and in my view the bank was dragged in as a defendant in suit no. 34 of 1984 because the disputed shares relate to the bank's shares.

What are the main complaints of the plaintiffs in the present suit? The plaintiffs complained that in view of the defendant's dual position and interests in Ming Yueh and the bank, the defendant should not participate in the board's deliberations/decisions in respect of suit nos. 17 of 1989, 23 and 34 of 1984 like the lines of defence of the bank and the appointment of solicitors/senior Counsels etc. on the grounds of conflict of interests citing Article 73 of the memorandum and articles of association of the bank and breach of his fiduciary duty as a director which duty he owed to the bank and its shareholders.

It would be appropriate to note that an attempt was made by the parties in suit nos. 23 of 1984 and 34 of 1984 with the assistance of Bank Negara to work out what is termed "a global settlement" but such attempt failed resulting in the institution of suit no. 17 of 1989 and the present suit and perhaps more suits/applications will follow, each party trying "to outdo each other". It would appear to have resulted in a feud among the directors/shareholders which may not be in the ultimate interests of the bank.

(1) Locus Standi

The plaintiffs, it would appear, are suing in their capacities as registered shareholders of the bank. According to Mr. Wong, then the plaintiff will be caught by the rule in *Foss v. Harbottle*. However, Mr. Abraham submitted that the "proper plaintiff" aspect of the rule in *Foss v. Harbottle* does not apply where what is complained of is not a wrong to the company but an injury to the plaintiffs as members personally. If the plaintiffs' rights are infringed, they may sue in respect of those rights and the directors and majority members cannot stop them (see *Edwards v. Halliwell* [1950] 2 All ER 1064). The plaintiffs are alleging that their rights to attend and vote at a meeting and requisition an extra-ordinary general meeting or attend the annual general meeting are infringed by the injunction obtained by the defendant by virtue of his position and interests in Ming Yueh as well as the bank. In other words what the plaintiffs are alleging is that the defendant used Ming Yueh as the vehicle to frustrate the rights of the plaintiffs in the bank, that is, going by the back door what he could not possibly achieve by the front door. In support of the alleged rights of the plaintiffs as members of the bank, Mr. Abraham relied on Articles 41, and 45 to be read with Article 79 of the memorandum and article of the bank (see JK25). However, as I said earlier, on 2

September 1987 I set aside the interim injunction order obtained by Ming Yueh in suit no. 17 of 1989, thus the plaintiffs' alleged rights are no longer infringed. As said earlier by me, I am advised that there has been no appeal against my said order though initially, Mr. Wong, Counsel for Ming Yueh indicated that Ming Yueh intended to appeal. Therefore the allegations of infringement of the plaintiffs' rights as members are now only academic. Mr. Wong seemed to suggest that the defendant has nothing to do with the action of Ming Yueh in suit no. 17 of 1989 as Ming Yueh exists as a legal entity of its own. But it should be noted that the defendant is the chairman, director and shareholder of Ming Yueh and this fact is not disputed. Such argument of Mr. Wong, in my view, is a fallacy as according to *Gower's Principles of Modern Company Law*, 4th Edn., at p. 210, it is stated:

> Here it must be suffice to say that those controlling the management of the company (normally the directors or managing director) are treated as the company's "brain" and whenever the brain functions, there resides the company.

Further at p. 211, quoting Lord Haldome's speech in *Lennard's Carrying Company v. Asiatic Petroleum* [1915] AC 705, Lord Denning LJ in *HL Bolton Co. v. TJ Graham & Sons* [1956] 3 All ER at p. 630 held:

> A company may in many ways be likened to a human body. They have a brain and a nerve centre which controls what they do. They also have hands which hold the tools and act in accordance with directions from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what it does.

In view of the defendant's position in Ming Yueh there is no doubt in my view that he is "the brain" in Ming Yueh instituting suit no. 17 of 1989 (see the allegations of the second plaintiff in JK 29 wherein he as a director of Ming Yueh was not consulted regarding the institution of suit no. 17 of 1989 by Ming Yueh. The second plaintiff resigned as a director of Ming Yueh on 10 May 1989 - (see JK 29).

In view of what I said earlier regarding the alleged infringement of the plaintiffs' rights by virtue of the setting aside of the interim injunction order obtained by Ming Yueh, I do not think that the plaintiffs can avail themselves of the exception to the rule in *Foss v. Harbottle* that is, infringement of members' personal rights. To say the least, the plaintiffs had taken upon themselves to file this proceeding without waiting for the outcome of the application by the bank to set aside the interim injunction as such result may have a bearing on what they are now complaining of in the present proceeding about infringement of their personal rights as members.

As Mr. Abraham conceded that the present action of the plaintiffs is not a derivative action it is not necessary for me to dwell into this aspect. In any event there is no evidence shown that the plaintiffs have taken the necessary steps as required before a derivative action can be instituted.

It only now remains for me to consider the issue of conflicts of interests and fiduciary duty of the defendant as a director of the bank *vis-a-vis* the issue of the disputed 785,699 shares which Ming Yueh is claiming and of which the defendant has interest in Ming Yueh as a chairman, director and shareholder. Under Article 73 of the bank, a director may contract with and be interested in any contract made with the company but the interest of the director on such contract be declared to the board but no director shall vote in respect of any contract or arrangement in which he shall be interested.

Now, the memorandum and articles of association constitute a contract between the members *inter se*. The contract is deemed to contain covenants that each member will observe all the provisions of the memorandum and articles (see s. 33(1) of the Companies Act 1965). Therefore every member has a personal right to have the terms of the memorandum and articles observed. Since this right is personal there is no room for the application of the rule in *Foss v. Harbottle* in an action to enforce the memorandum or articles. In fact a member may enforce his right to have the provisions of the memorandum and articles observed by injunction, either mandatory or prohibitory. The action may be brought directly against the other members, and the company does not have to be joined as a party (see *Rayfields v. Hands* [1960] Ch 1. A member's rights and liabilities under the articles of association are a matter of contractual obligation. (See *Wong Kim Fatt v. Leong & Co. Sdn. Bhd.* [1976] 1 MLJ 140). (See pp. 96 and 97 of *Walter Woon on Company Law*). In view of the defendant's position and interests in Ming Yueh and the bank which are not disputed, is it then right for the defendant to deliberate and vote thereat in the bank's board meeting pertaining to suit nos. 17 of 1989, 23 of 1984 and 34 of 1984 for which Ming Yueh are parties without offending Article 73 of the memorandum and articles of association of the bank? Though the interest of the defendant is not concerned perhaps with a contract *per se* but Article 73 specifies "any contract or arrangement in which he shall be interested". The sale of the disputed 785,699 shares could very well, in my view, be within the purview of "arrangement" for which the defendant is interested by virtue of his interests in Ming Yueh. According to '*The Conduct of Meeting*', 22nd Edn. by John Yelland at p. 55, "The smallest conceivable conflict of interest will be sufficient to bring this rule into operation". According to Robert R. Pennington's *Company Law*, 5th Edn., at p. 727 it is opined as follow:

> The dividing line between personal and corporate rights is very hard to draw, and perhaps the most that can be said is that the Court will incline to treat a provision in the memorandum or articles as conferring a personal right on a member only if he has a special interest in its observance distinct from the general interest which every member has in the company adhering to the terms of its constitution.

In the present proceeding, I am of the view that the plaintiffs as shareholders have a special interest in the observance of Article 73 as the defendant by virtue of his interest in Ming Yueh will have the advantage of taking part in the deliberation and decision on the lines of action to be taken by the bank in respect of the suits filed in Court which may be to the detriments of the bank/shareholders. Clearly the justice of the case requires the defendant to declare his interests and refrain from taking part and voting in respect of matters pertaining to those suits of which Ming Yueh is a party.

In the circumstances I am of the opinion that the plaintiffs as shareholders of the bank are the proper plaintiffs and they should have the *locus standi* to bring this action against the defendant to ensure that the provisions of Article 73 are strictly complied with by the defendant. I accordingly rule that the plaintiffs have the *locus standi* to institute the present proceeding.

(2) No cause of action.

In view of my finding that the defendant is in breach of his fiduciary duty and also acting in conflict of interest thereby offending Article 73 and which are so pleaded in the plaintiffs' amended statement of claim, surely such pleadings disclose a cause of action as against the defendant. I have no quarrel with the statement of law that the statement of claim must establish a substantive claim and that injunctions are merely ancillary reliefs. As such, with respect, I do not agree with the submission of Mr. Wong that reliefs of injunctions are merely

ancillary reliefs and as they do not have a peg to hold on, the present application of the plaintiffs cannot be maintained as I rule that there is a cause of action established by the plaintiffs.

In the result, I would dismiss the preliminary objection of the defendant and order for the hearing of the summons (Encl. 16) on a date to be fixed.

Also found at [1990] 1 CLJ 512